Annual Report 1974 Canadian Cellulose Company, Limited

1974

Annual General Meeting

April 25, 1975, 9:30 a.m.
Social Suite West, Hotel Vancouver, Vancouver, B.C.

Index

Corporate Information

BOARD OF DIRECTORS

E. Bertram Berkley†
Chairman and President, Tension Envelope Corporation, Kansas City

Alan S. Gordon*
Consultant, Merrill Lynch, Royal Securities Limited, Montreal

Ronald M. Gross*
President and Chief Executive Officer, Canadian Cellulose Company, Limited, Vancouver

W. C. Raymond Jones
Chairman, British Columbia Cellulose Company, Vancouver

Max Litvine
Managing Director, Compagnie Bruxelles Lambert, Brussels

Charles C. Locke, Q.C.†
Partner, Ladner Downs, Vancouver

John H. Spicer
System Vice-President, Planning and Administration, Canadian National Railways, Montreal

Ira D. Wallach*
Chairman and Chief Executive Officer, Gottesman and Company Inc. and Central National Corporation, New York

Donald N. Watson*†
President and Chief Executive Officer, Pacific Western Airlines Ltd., Vancouver

** Member of Executive Committee — Chairman, Donald N. Watson*
† Member of Audit Committee — Chairman, Charles C. Locke, Q.C.

OFFICERS

Ronald M. Gross
President and Chief Executive Officer

Donald P. Best
Senior Vice President, Operations

Frank X. Guimond
Senior Vice President, Engineering and Development

Roger J. Duncan
Vice President, General Counsel

Herschell F. Huff
Vice President, International Pulp Marketing

Gordon R. McLachlin
Vice President, Lumber Operations

Roy W. Murphy
Vice President, Personnel and Administration

Clive B. Symons
Vice President, Treasurer

William H. Vaughan
Vice President, North American Pulp Marketing

Alan K. Wilkinson
Secretary

OPERATIONS

John N. Babcock
Manager, Kitwanga Lumber Operations

Orjan Burchardt‡
Vice President, Interior Pulp Operations

Robert E. Davis
Manager, Pohle Lumber Operations

Edward C.J. Higgs
Manager, Interior Lumber Operations

G. Edward Lloyd
Manager, Interior Woods Operations

Leonard S. Steel
General Manager, Northern Pulp Operations

W. Frederick Waldie
Manager, Northern Woods Operations

‡ Also an Officer

CORPORATE MANAGEMENT

A. V. (Bill) Backman
Director of Planning and Forestry

F. D. Giles
Operations Controller

Harry R. Papushka
Director, Supply and Distribution

Samuel H. Smillie
Director, Labour Relations

R. W. Sweeney
Director of Engineering

Robert E. Swenarchuk
Director, Public Relations

PLANTS AND OFFICES

Corporate Office
1200-1111 West Hastings Street
Vancouver, B.C. V6E 2K2

Sales Offices
Montreal, P.Q.
Brussels, Belgium

Kraft Pulp Mills
Prince Rupert, B.C.
Castlegar, B.C.

Sulphite Pulp Mill
Prince Rupert, B.C.

Lumber Mills
Terrace, B.C.
Kitwanga, B.C.
Castlegar, B.C.

Woods Operations
Terrace, B.C.
Nakusp, B.C.

CORPORATE DATA

Transfer Agent and Registrar
Montreal Trust Company,
466 Howe Street, Vancouver, B.C. V6C 2A8
and branches in Toronto and Montreal

Stock Listings
Montreal, Toronto and Vancouver Stock Exchanges

Auditors
Coopers & Lybrand,
28th Floor, 1055 West Georgia Street,
Vancouver, B.C. V6E 3R2

Principal Subsidiary and Affiliated Companies
Babine Forest Products Limited (24% owned)
Canadian Cellulose International, S.A.
Celgar Properties Limited
Celtran Equipment Limited
Colcel Properties Limited
Haseldonckx, S.A. (50% owned)
Les Papeteries de Gastuche, S.A. (43% owned)
Pohle Lumber Co. Ltd.
Twinriver Timber Limited

Highlights

	1974	1973
Earnings		
Net sales	$191,501,000	133,801,000
Earnings before taxes and extraordinary item	54,591,000	13,278,000
Earnings before extraordinary item	28,991,000	7,078,000
Net earnings	50,866,000	12,318,000
Per share		
Earnings before extraordinary item	$ 2.38	.58
Net earnings	4.17	1.01
Cash flow from operations before extraordinary item	3.29	1.54
Dividends	.05	—
Financial position at end of year		
Working capital	$ 52,613,000	13,174,000
Total assets	148,180,000	113,207,000
Long term debt	54,291,000	61,426,000
Shareholders' equity	58,860,000	8,603,000
Additional information		
Expenditures on fixed assets	$ 14,576,000	9,441,000
Wages, salaries and employee benefits	48,300,000	37,290,000
Number of employees at end of year	3,197	3,022
Number of registered shareholders at end of year	6,337	6,387


Ronald M. Gross, President

To Our Shareholders and Employees —

In 1974, Canadian Cellulose realized significant improvement in sales and earnings.

Net sales for the year increased to $191.5 million from $133.8 million and earnings from our business operations amounted to $29 million or $2.38 per share, after making provision for income taxes, compared to $7.1 million or 58 cents per share in 1973.

Net earnings after an extraordinary tax credit were $50.9 million or $4.17 per share compared to $12.3 million or $1.01 per share.

During the year, the company's financial position improved. Working capital at year-end amounted to more than $52 million, compared to approximately $13 million at the end of 1973, and the ratio of current assets to current liabilities improved from 1.3:1 to 2.5:1. Funds generated from operations amounted to $62 million, and after normal repayments on first mortgage bonds of approximately $6 million, expenditures on fixed assets of approximately $15 million and the initial dividend payment, working capital increased by more than $39 million.

Approximately $14 million of this increase was used to finance increases in inventories, with most of the remainder being applied to repay bank loans and improve the company's cash position. Approximately $6 million of the inventory increases was caused by higher costs; the remaining $8 million was represented largely by increases in quantities over the unusually low pulp inventory levels at the end of 1973.

The sales and earnings performance can be attributed to higher prices and the strong demand for pulp that prevailed throughout the year. On the other hand, costs increased in all areas of operations to an extent never before experienced.

Lumber products accounted for less than 20 percent of sales and did not contribute materially to earnings in the last half, when

prices and demand fell to levels not experienced for some years.

Throughout the year, softwood bleached kraft pulp was in short supply in all world markets.

As one of the few major pulp producers in the world without forward integration, the company was a sought-after supplier by non-integrated paper makers. Additional long-term contracts were developed with a broad range of customers and our pulp now is marketed substantially on this basis in more than 24 countries.

The development of these customer relationships based on continuity and reliability is consistent with our belief that long-term commitments can be beneficial both to our customers and to the company.

In November, your Directors adopted a policy of quarterly dividends and an initial payment of five cents per share was made in December. Subsequently, at the February meeting of the Board, a first quarter dividend of seven and one-half cents per share was declared, payable on March 24 to shareholders of record on March 10, 1975.

Capital expenditures during the year amounted to $14.6 million, an increase of $5.2 million over 1973. Projects undertaken in 1974 involved expenditures of $700,000 for improved working conditions, $3.2 million for profit improvement programs, $4.4 million for logging roads, $5.2 million for equipment replacement and $1.1 million for pollution control.

Included in the profit improvement program for 1974 was an expenditure of $340,000 as part of the company's contribution to the sawmill construction costs of Babine Forest Products Limited, at Burns Lake. The project, which is scheduled to be in operation by mid-1975, is a joint venture with Weldwood of Canada Limited and Eurocan Pulp & Paper Co. Ltd., as major partners, and the Burns Lake Native Development Corporation which holds an eight percent interest. The company's 24 percent equity participation in the consortium was made to provide for a long-term supply of residual by-product wood chips for the Prince Rupert pulp operations.

Major studies of the wood resources available to the company were completed at year-end and will provide the basic data for more detailed examination of expansion possibilities. The feasibility of a number of alternative projects is being examined with a view to achieving a satisfactory return on investment and the most efficient use of the natural resources. Consistent with the company's prudent financial policy, any development undertaken will require a substantial "down payment" from funds generated by our existing operations.

In these times of severe inflation, it is vitally important to identify real profits and return on investment. Absolute dollar earnings on a historical cost basis are less meaningful when used in attempting to analyze the economics of investments of the magnitude required today, particularly in the forest products industry.

As a supplement to the conventional financial statements in this report, and for information purposes only, we have prepared inflation-adjusted statements which attempt to focus on this complex problem.

The level of earnings, asset values and shareholders' equity in terms of 1974 dollars, which are shown in the supplementary statements, are based on price-level adjustments and reflect real values more accurately than statements based on historical cost.

The constraining factor of inflation on new investment may have one immediate beneficial effect on the industry and on the company. In the past, whenever world demand for forest products approached capacity, as happened in the pulp and paper sector in 1973 and 1974, many companies launched major expansion programs. The result was to over-produce, which depressed prices and put the industry generally into unacceptable rates of return.

This is not a factor in the current cycle because little new pulp capacity is scheduled to come on stream during the next three years.

In late November, the provincial government enacted the Timber Products Stabilization Act, which authorized the establishment of a Forest Products Board of British Columbia and which enables the government to set prices for wood

chips. Subsequently, in January, 1975, a general price of $35.00 at the sawmill per unit of chips was established for the first quarter of the year. Price levels beyond the end of March are uncertain.

The increase in chip costs, however, again will be substantial as the company annually purchases more than 200,000 units of residual chips from independent sawmills in the province. During 1974, the price for chips rose from an average of $10 per unit early in the year, to $28 per unit at year-end.

The impact of government on the forest industry is dramatic and we look to both the federal and provincial governments for stable policies that will encourage the industry to develop its full potential and continue its significant contribution to the economy. Stumpage, property and income taxes for our company alone amounted to $14.3 million in 1974, compared to $12.7 million in 1973.

The Board of Directors was increased in mid-year with the appointment of W.C.R. Jones, Chairman of the Board of Directors of British Columbia Cellulose Company, as an additional Director.

All those associated with the company were saddened to learn of the death, on October 21st, of Dr. Harry L. Purdy, who, during his service from June, 1973, made a substantial contribution to the company, both as a Director and as Chairman of the Executive Committee of the Board.

Senior management appointments during the year were those of D. P. Best as Senior Vice President, Operations, and R. J. Duncan as Vice President, General Counsel. Mr. Best was formerly a Vice President of Georgia Pacific Corporation and President of K. V. P. Canada Ltd., and Mr. Duncan was formerly a partner in a major Vancouver law firm.

Outlook

Economic conditions for the remainder of 1975 are unclear, and for this reason it is difficult to predict the precise strength of pulp and lumber markets. If the general economic picture does not improve, we would expect to curtail production to some extent in order to balance inventories. The long-term potential for our company appears, however, to be good.

In 1975, for the first time in recent years, all organized forest workers in the province will be negotiating for new collective agreements at the same time. The company will be actively involved in industry-wide negotiations with the Pulp, Paper and Woodworkers of Canada and with the International Woodworkers of America. In total, 12 contracts with four unions will be expiring in this period and will directly affect all company operations ranging from the woods sector through to sawmilling and pulp production.

We anticipate that these concurrent negotiations will be difficult considering the divergent profit levels within the different sectors of the industry, particularly the depressed markets for wood products.

Cost-of-living allowances negotiated in the collective labour agreements during 1974 provide protection for the real purchasing power of the dollar. It is hoped labour will responsibly relate wage demands to productivity and the current Canadian economic condition and recognize that a real return on invested capital is essential for job maintenance and continued job growth.

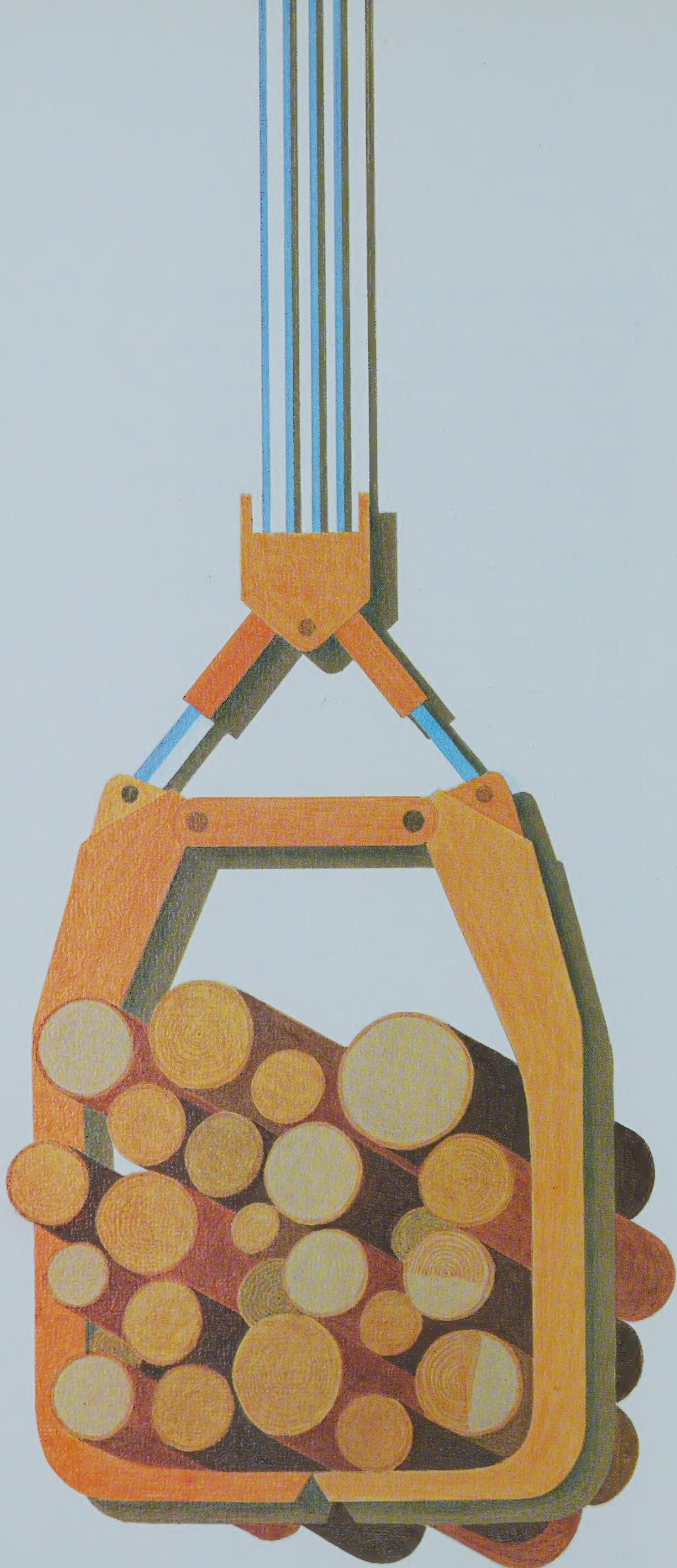
More critical than at any previous time is the urgent need for government, labour and industry to jointly develop a new compact – a mutually acceptable framework that will permit industry to invest capital which will yield a return and in so doing, provide the jobs, government revenues and the general economic structure for a healthy economic and social environment in British Columbia and in Canada.

On behalf of the
Board of Directors,

R M Gross

Ronald M. Gross
President and Chief Executive Officer

Vancouver, B.C.
February 25, 1975



Operations Review

Logging and Forestry

The company's logging operations, located along the Nass and Skeena river systems of north-western British Columbia and along the Columbia River basin in the southern interior, produced 1,297,000 cunits of logs (a cunit is 100 cubic feet) compared to 1,451,000 cunits in 1973. More than half of the volume was produced for the company by independent contractors.

Lower log requirements, due to higher-than-normal inventory at the beginning of 1974, accounted for reduced production at the northern woods operations, where volume dropped to 933,000 cunits from 1,147,000 cunits. Heavy snowfalls in the early part of the year, a forest fire in August, a flash flood in October, which caused damage to roads and bridges, and several work stoppages interrupted the continuity of operations.

In the interior, production reached 364,000 cunits, compared to the 1973 volume of 304,000 cunits.

Rising costs affected all logging operations and is a matter of continuing concern. Major increases occurred in equipment rental and capital costs, and in wages and fuel charges.

New forest management guidelines imposed by the provincial Forest Service for the industry also have added sharply to the general pressures on costs. As an example, road building costs in the interior woods operations rose to an average of $21,700 per mile in 1974 from $11,900 in 1973, and from $9,900 in 1972. A substantial part of the increase is due to the new requirements for improved road alignment and grades and more complete waste wood disposal along roads.

The provincial forest management policy now takes into account the various potential uses of the resource, and more governmental agencies are involved in the processing and approval of proposed road building and timber harvesting programs. As a result, severe delays have been encountered in obtaining permits.

Use of cable-logging systems is being extended to meet more rigid environmental requirements for steep-slope harvesting. Two additional grapple yarders, costing nearly $250,000 each, were ordered for the northern region, bringing the number of these units in the Terrace area to five, and one unit was purchased for the interior operations at Nakusp. Also in the interior, experiments were continued with new types of mechanical falling equipment.

Reforestation is carried out by the company to supplement natural regeneration of cut-over lands. At the northern operations, nearly 2,000 acres were replanted with 850,000 seedlings. In the interior, however, only 96,000 seedlings out of a forecast requirement of 230,000 were available and little more than 200 acres were re-planted. This shortfall was caused by seedling frost damage and is expected to be overcome by an expanded 1975 program, during which more than 2,000 acres are scheduled to be planted with 925,000 seedlings.

New inventories of standing timber in the two tree farm licences under CanCel's management were completed. The updated data will assist in planning for the most effective utilization of these resources.

Lumber Operations

The company's lumber facilities operated at a reasonably satisfactory production level notwithstanding the generally poor lumber market.

Production at the company's three sawmills, located at Castlegar, Terrace and Kitwanga, amounted to 243 million board feet compared to 254 million board feet in 1973. The lower volume reflected the sharp drop in demand for wood products in the United States, where housing starts fell from 2.1 million in 1973 to 1.4 million in 1974, and which, at year-end, were at an annualized rate of 868,000 starts.

Lower prices and higher costs accompanied the decline in demand in the United States and other areas where our lumber is sold. By December, the average price was approximately $45 per thousand board feet lower than that realized at the beginning of the year, while the cost of manufacturing lumber rose in the same period by approximately $20 per thousand board feet.

The Castlegar sawmill in the southern interior of the province has a maximum annual capacity of 129 million board feet. Production at this facility in 1974 reached 117 million board feet compared to production of 100 million board feet in 1973, when volume was adversely affected by industry-wide work stoppages.

A major capital project at the Castlegar operation was the installation of a double-arbor edger costing $485,000, which was completed in December. The unit replaced equipment which had become obsolete and will improve operating efficiency.

The Castlegar sawmill has an unusual design feature that permits simultaneous processing of two wood species. The mill incorporates two separate headsaws, one of which saws fir,

hemlock or cedar, while the other saws pine or spruce. Subsequent processing to the finished market lumber stage is along a common system.

The quality kiln-dried lumber produced at Castlegar is marketed principally in the midwest and southern areas of the United States. The mill specializes in "mixed-car" sales which allow customers a wide degree of flexibility in boxcar-sized orders. Up to 50 selected sizes, species and grades can be specified in one boxcar and this factor contributed substantially to continuity of sales in the difficult 1974 lumber market.

The company's northern lumber operations at Terrace and Kitwanga produced 126 million board feet compared to 154 million board feet in 1973.

These mills, which have a combined capacity of 162 million board feet, both feature equipment capable of sawing dimension lumber and converting waste material to chips in a single operation. The "Chip-N-Saws" manufacture a high percentage of each log into lumber and pulp chips and are well suited to processing smaller logs now being harvested under close utilization standards.

A $2 million capital expenditure program completed during the year at the Terrace mill resulted in increased recovery of lumber and pulp fibre and improved environmental control.

Like the interior operations, output from the northern mills is marketed principally in the midwest and southern United States.

With the recent and planned improvements to its lumber converting facilities, the company is in an excellent position to benefit from an improved lumber demand. In addition to consolidating its strong position in United States markets, the company is actively investigating the feasibility of extending sales to offshore markets.

Pulp Operations

The kraft and sulphite pulp mills located at Prince Rupert on the northwestern coast of the province, and the kraft mill at Castlegar in the southern interior, operated at generally improved levels during 1974.

Sulphite production amounted to 156,200 tons compared to 140,500 tons in 1973. Total kraft production increased to 409,000 tons from 377,700 tons.

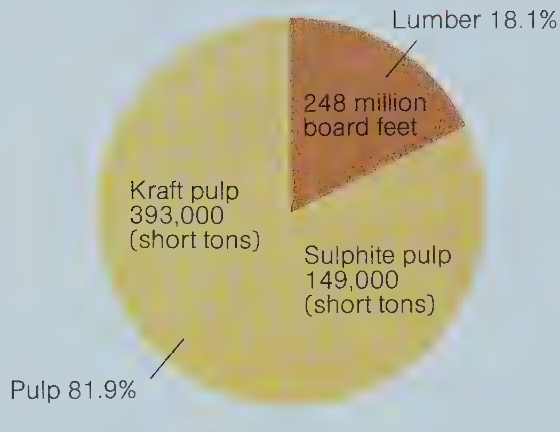
The higher production reflects a partial recovery from the industry-wide labour disputes of 1973. Although there were shutdowns at both northern and interior operations as a result of labour disputes during 1974, these did not approach the severity of the 26 and 72 day strikes of the previous year.

Cost increases were significant. Natural gas and fuel oil rose by $3.5 million to $8.5 million. The cost of purchased chips, required to balance the company generated supply, increased by $1.1 million to $4.4 million, and chemicals and other supplies also increased.

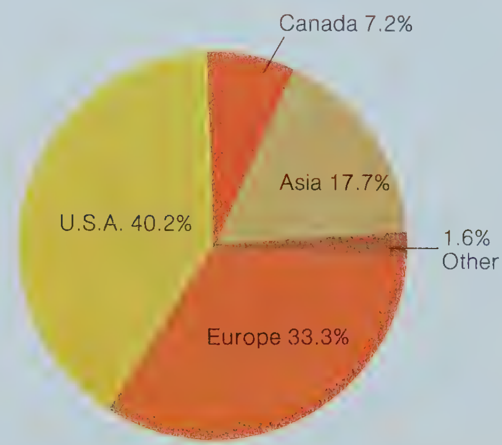
Major emphasis was placed during 1974 on finalizing a comprehensive environmental control program to meet the requirements of provincial and federal regulatory authorities by specified times.

The plan calls for expenditures to 1983 in the order of $40 million (in 1974 dollars) excluding the potentially large costs for effluent control at the Prince Rupert sulphite mill. Plans for the future of this latter operation are under review. Although formal approval for the overall program has not been received from the appropriate agencies, orders have been placed for some equipment. Costs in 1974 were $1.1 million and expenditures planned for 1975 amount to $2.4 million.

Sales by major product-1974



Pulp sales by market area-1974



At the Castlegar pulp mill, major attention currently is being directed to air emissions. Installation of an improved recovery stack scrubber, designed to exceed requirements of the provincial Pollution Control Branch for particulate emissions, will be completed in 1975. The device, which will be the third such installation in North America, will also reduce the haze that can occur in the region of the mill under certain weather conditions.

At the Prince Rupert operations, current emphasis is on effluent control. The company is conducting a comprehensive study to evaluate the environmental impact of the sulphite mill's

effluent on receiving waters. Modifications already have been made to the company's two mile effluent pipeline to improve dispersal in ocean waters.

An improved liquid discharge system at the Prince Rupert kraft mill, and woodroom installations designed to upgrade effluent quality to comply with regulatory objectives in this area, will be completed in 1975.

The northern mills' capacity to generate energy is being expanded to improve utilization of waste fibre and to reduce the impact of escalating costs of fuel oil and natural gas. Costing in excess of $1 million, the modernized facilities will consume wood bark and other combustible waste generated from the pulp operations. In addition to processing waste material presently being produced, the company is studying the possibility of reclaiming stockpiled waste fibre accumulated on the site since commencement of operations in 1951.

Total utilization of waste fibre for power generation has been a feature of the Castlegar pulp mill and adjoining sawmill since the start-up of that complex in 1961. Savings achieved by the present use of waste fibre compared to equivalent natural gas requirements are estimated at $1.5 million annually.

Pulp from the kraft and sulphite mills at Prince Rupert is shipped from deepsea docks at the site to a broad range of customers throughout the world and by rail to North American markets.

The softwood kraft output from the Castlegar mill is shipped by rail to North American customers, principally in the United States.

The sulphite Columbia-brand pulps include dissolving grades, which are used as the basic raw material for acetate and rayon textiles and cellophane film, and paper grades which are used in some fine printing and writing papers.

The high quality Skeena and Celgar brand bleached kraft pulps produced by the company find their way into a variety of paper-related products including cartons, tissue products and other consumer goods and, like the sulphite paper grades, into fine printing and writing papers.

Employee Relations

The company employs more than 3,200 persons in a wide variety of jobs which require increasingly complex trade, vocational and professional skills.

The past year was characterized by major efforts in contract negotiations, settlement of industrial disputes and implementation of employee benefit, communication and development programs. Total wages, salaries and employee benefits exceeded $48 million, representing an overall increase of approximately 29 percent over 1973 when lengthy strikes resulted in lower-than-normal wage costs.

In 1974, a one-year contract was negotiated with the International Woodworkers of America, and unilateral industry-wide mid-contract wage adjustments were granted to pulp employees to achieve a comparable rate structure among the sawmill, woodlands and pulp sectors of the forest products industry.

The collective agreement with the IWA provided for a 12 percent general wage increase with a minimum increase of 65 cents per hour. The agreement also provided increases for specific jobs above the base rate of $5.10, a cost-of-living allowance tied to changes in the Consumer Price Index and expanded benefit improvements, such as dental care and increased vacation entitlements.

During the year a total of 117 operating shifts, amounting to more than 27,000 manhours, were lost as a result of labour disputes throughout the operating divisions. Although this lost time was less than that experienced in 1973, which was a negotiating year with the pulp unions, it is significant to note that 44 percent of the lost time resulted from illegal work-stoppages and walkouts.

Salary increases were implemented to maintain the company's policy of providing a competitive salary structure and recognizing both individual performance and the relative contribution of each job to over-all company effort. The company also has improved the salaried employee benefits plan by increasing benefits

and eliminating employee contributions. Pension benefits under the optional salaried retirement plan were increased and required employee contributions reduced.

Continuing attention has been given both to employee communications, through general information programs, and to community relations, through increased company and employee participation in civic projects.

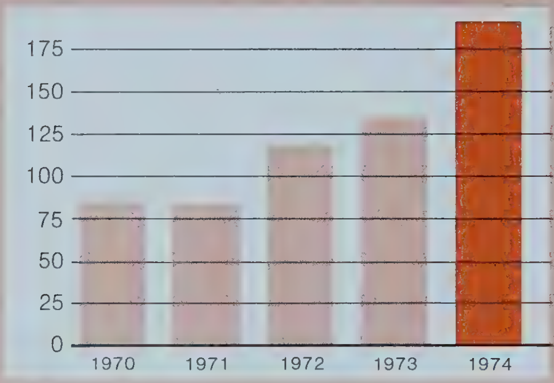
Although the severity of industrial accidents decreased in 1974, the high frequency of lost-time cases was unsatisfactory. General employee turnover was lower, indicating an improvement in stability, although the high level of turnover in the northern operations is of continuing concern. Specific programs are being implemented to lessen these problems.

Summary by quarter

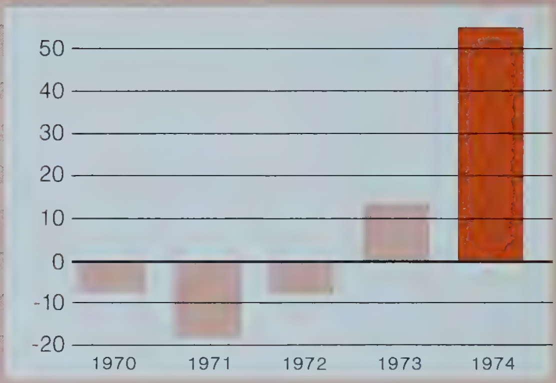
(Thousands)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net sales	$ 38,992	53,926	47,728	50,855
Earnings before taxes and extraordinary item	8,868	14,345	15,478	15,900
Provision for income taxes	4,170	6,900	7,380	7,150
Earnings before extraordinary item	4,698	7,445	8,098	8,750
Extraordinary item	3,845	5,800	6,205	6,025
Net earnings	$ 8,543	13,245	14,303	14,775
Per share				
Earnings before extraordinary item	$ .39	.61	.66	.72
Net earnings	$ .70	1.09	1.17	1.21

Five years at a glance (millions of dollars)

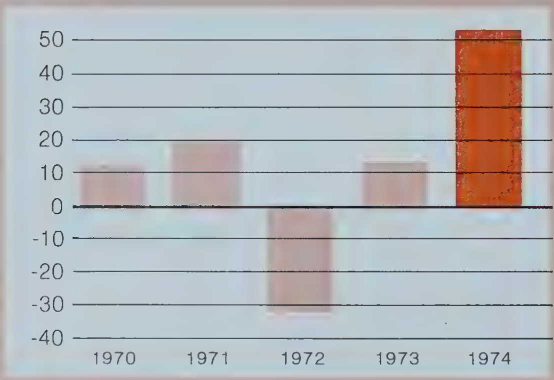
Net sales



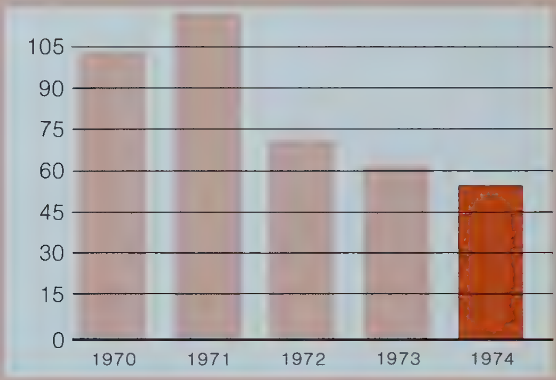
Earnings before taxes and extraordinary items



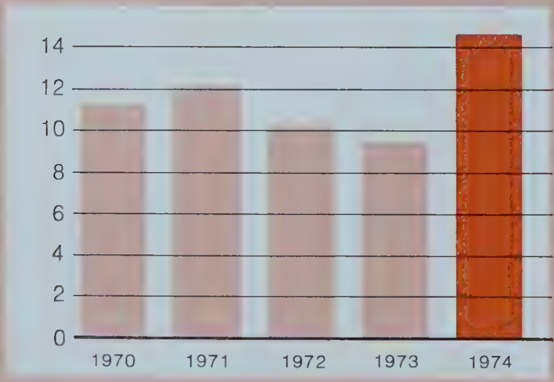
Working capital at year-end



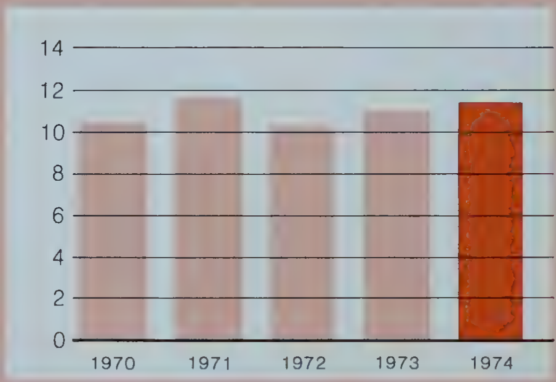
Long term debt at year-end



Expenditures on fixed assets



Depreciation expense



Consolidated Statement of Earnings

	1974	1973
	(Thousands)	
Revenues		
Net sales	$ 191,501	133,801
Other income	1,302	334
	192,803	134,135
Cost and expenses		
Cost of goods sold	129,149	111,522
Selling and administration	4,775	3,993
Long term debt interest	3,585	3,957
Other interest	703	1,385
	138,212	120,857
Earnings before taxes and extraordinary item	54,591	13,278
Provision for income taxes	25,600	6,200
Earnings before extraordinary item	28,991	7,078
Income tax reduction on application of prior years' losses (note 5)	21,875	5,240
Net earnings	$ 50,866	12,318
Per share		
Earnings before extraordinary item	$ 2.38	.58
Extraordinary item	1.79	.43
Net earnings	4.17	1.01

Consolidated Statement of Deficit

	1974	1973
Deficit at beginning of year	$ 60,147	83,964
Net reduction resulting from reorganization (note 2)	—	11,499
Net earnings for the year	50,866	12,318
	9,281	60,147
Dividends	609	—
Deficit at end of year	$ 9,890	60,147

Consolidated Balance Sheet at December 31

ASSETS

	(Thousands) 1974	1973
Current assets		
Cash and bank deposit receipts	$ 18,996	3,612
Accounts receivable	21,358	18,950
Inventories (note 3)	47,201	33,686
Prepaid expenses	87	104
	87,642	56,352
Investments and deposits		
Investment in 50% owned company	2,024	1,624
Timber deposits and other investments	1,345	1,037
	3,369	2,661
Property, plant and equipment		
Timber cutting rights, roads and related facilities	30,637	26,293
Buildings, machinery and equipment	231,928	225,019
	262,565	251,312
Less: Accumulated depreciation, amortization and depletion (note1(d))	206,390	198,120
	56,175	53,192
Land	994	1,002
	57,169	54,194
	$ 148,180	113,207

LIABILITIES

		(Thousands)
	1974	**1973**
Current liabilities		
Bank loans	$ —	13,124
Accounts payable and accrued liabilities	24,603	23,937
Logging taxes payable (note 5)	4,271	—
Current portion of long term debt	6,155	6,117
	35,029	43,178
Long term debt		
First mortgage bonds (note 4)	53,903	59,892
Other	388	1,534
	54,291	61,426
SHAREHOLDERS' EQUITY		
Capital Stock (note 6)		
Non-Voting Shares without par value. Authorized 60,000 shares; issued 39,750 shares	39,750	39,750
Common Shares without par value. Authorized 24,318,119 shares; issued 12,151,453 shares	29,000	29,000
	68,750	68,750
Deficit	9,890	60,147
	58,860	8,603
	$ 148,180	113,207

Signed on behalf of the Board

Director *Director*

Consolidated Statement of Changes in Financial Position

	(Thousands) 1974	1973
Source of funds		
From operations		
Earnings before extraordinary item	$ 28,991	7,078
Charges to earnings not involving use of funds		
Depreciation, amortization and depletion	11,403	10,786
Deferred logging taxes	—	895
Other	(323)	(21)
	40,071	18,738
Income tax reduction on application of prior years' losses	21,875	5,240
	61,946	23,978
Proceeds from sales of fixed assets	130	671
Contribution and other adjustments resulting from reorganization (note 2)	—	41,645
	62,076	66,294
Application of funds		
Expenditures on fixed assets	14,576	9,441
Purchase of leased equipment	—	3,475
Dividends	609	—
Reduction of long term debt		
First mortgage bonds	5,989	6,112
Other	1,169	1,226
Other investments	294	229
	22,637	20,483
Net increase in working capital	39,439	45,811
Working capital (deficiency) at beginning of year	13,174	(32,637)
Working capital at end of year	$ 52,613	13,174

Notes to the Consolidated Financial Statements

1. Significant Accounting Policies

(a) Principles of consolidation
The consolidated financial statements include the accounts of Canadian Cellulose Company, Limited and its subsidiaries, all of which are wholly-owned.

The investment in Haseldonckx, S. A. (50% owned), including its subsidiary, Les Papeteries de Gastuche, S. A., is accounted for on the equity basis.

(b) Foreign exchange
Current assets and current liabilities in foreign currencies are translated into Canadian dollars at the rates of exchange in effect at the end of each year. Long term debt has been translated into Canadian dollars at the rate of exchange prevailing at June 29, 1973, the date of reorganization (note 2). Income and expenses of foreign subsidiaries are translated at the average exchange rates for each year.

(c) Inventories
Inventories of pulp and lumber are valued at the lower of average cost or net realizable value. Other inventories are valued at the lower of average cost or replacement cost.

(d) Property, plant and equipment
Property, plant and equipment is stated at cost.

As a result of the reorganization on June 29, 1973 (note 2), property, plant and equipment was written down by $75,485,000, of which $9,964,000 was applied against the net book value of specific assets and $65,521,000 was added to accumulated depreciation, amortization and depletion.

Depreciation, amortization and depletion, other than for the sulphite mill, is computed on original cost as follows:

Pulp mills	4% composite rate on a straight-line method
Sawmills	4% to 6% composite rates on a straight-line method
Logging equipment	10% to 20% diminishing balance method
Timber cutting rights, roads and related facilities	production derived as a proportion to estimated total production available from such assets

The sulphite mill was written off in 1971 and annual capital expenditures incurred since then have been expensed as depreciation in the year incurred.

(e) Earnings per share
Earnings per share have been calculated on the basis of 12,191,203 shares, the number of shares outstanding since the June 29, 1973 reorganization.

2. Reorganization

Pursuant to an agreement dated as of April 2, 1973 and ratified by the British Columbia Cellulose Company Act, certain assets and liabilities of Columbia Cellulose Company, Limited (Colcel) were combined on June 29, 1973 with those of Canadian Cellulose Company, Limited (CanCel), formerly the principal operating subsidiary of Colcel. Colcel ceased to be a shareholder of CanCel. In addition, CanCel was required under the agreement to write down its fixed assets and changes were made to its capital.

The 1973 earnings and changes in working capital shown for comparative purposes include the consolidated figures of Colcel from January 1 to June 29, 1973 since all the operations formerly carried on by Colcel and its subsidiaries have been combined with those of CanCel. Where applicable, minor reclassifications have been made to the 1973 comparative statements to conform with the 1974 presentation.

3. Inventories

	(Thousands) 1974	1973
Logs, pulp chips and other raw materials	$30,004	22,514
Pulp and lumber	12,109	7,163
Supplies	5,088	4,009
	$47,201	33,686

4. Long term debt

First mortgage bonds, payable in U.S. funds, excluding the portion payable within one year which is included in current liabilities:

	(Thousands) 1974	1973
6-1/8% First Mortgage and Collateral Trust Bonds, due January 2, 1981 with annual sinking fund instalments. (1974 U.S. $24,000,000; 1973 U.S. $28,000,000)	$23,957	27,950
5-3/8% First Mortgage and Collateral Trust Bonds, due July 1, 1985 with annual sinking fund instalments. (1974 U.S. $30,000,000; 1973 U.S. $32,000,000)	29,946	31,942
	$53,903	59,892

The Province of British Columbia has unconditionally guaranteed payment of the principal and interest on the bonds.

Principal payments required on long term debt through 1979 are:

	(Thousands)
1975	$6,155
1976	6,425
1977	6,425
1978	6,425
1979	6,425

5. Income Taxes

In certain years before 1974, the company incurred cash losses and recorded in its accounts depreciation, including extraordinary write-downs of fixed assets, in excess of the amounts which it claimed for income tax purposes. The resulting potential tax benefits were not recognized in the accounts of those years because of the uncertainty of their ultimate realization. In 1974 a benefit of $21,875,000 has been realized because the company will claim for tax purposes sufficient of such prior years' losses and depreciation charges to eliminate liability for all income taxes other than logging taxes for the year.

The income tax value of the depreciable assets of the company at December 31, 1974 exceeds the value recorded in the accounts by approximately $70,000,000, which represents potential future tax benefits of approximately $32,000,000. Such benefits will be recorded in future years to the extent that the excess value may be applied against future years' taxable earnings. The maximum extent that the excess value may be applied in a particular year depends upon the maximum rate of depreciation allowed for income tax purposes and other factors. The maximum potential tax benefit available for 1975 is presently estimated to be approximately $16,000,000.

6. Capital Stock

Other than with respect to voting, the Common Shares and Non-Voting Shares are equal and carry the same rights including the right to payment of dividends and distributions of the same amount per share.

Under a stock option plan adopted November 30, 1973, 100,000 Common Shares are reserved for issue to key employees, the purchase price per share being the market value at the date of the grant of options under the plan. The options are for a term of ten years from date of grant and are exercisable after one year to the extent of 20% a year on a cumulative basis. At December 31, 1974, there were outstanding options to purchase 93,200 Common Shares exercisable at prices ranging from $4.325 to $6.375 per share. These options were granted in 1974 and expire in 1984 or upon termination of employment of the optionee, whichever is earlier.

7. Commitments and Contingent Liabilities

The company has agreed to invest up to a maximum of $2,000,000 in Babine Forest Products Limited. Advances to December 31, 1974 total $480,000.

The company has guaranteed bank loans of certain of its suppliers. As at December 31, 1974, the total of such loans outstanding and subject to guarantee was $715,000, against which a reserve of $465,000 has been provided.

8. Remuneration of Directors and Officers

The aggregate direct remuneration paid or payable to directors and senior officers amounted to $665,000 in 1974.

9. Subsidiary Companies

Calum Lumber Limited
Canadian Cellulose International, S. A.
Celgar Properties Limited
Celtran Equipment Limited
Colcel Properties Limited
High Arrow, S. A.
Nass, S. A.
Pohle Lumber Co. Ltd.
Twinriver Timber Limited

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Canadian Cellulose Company, Limited and subsidiaries as at December 31, 1974 and the consolidated statements of earnings, deficit and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the company as at December 31, 1974 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Coopers & Lybrand
Chartered Accountants

Vancouver, B.C.
February 7, 1975

Comment on Inflation

Financial statements based on historical costs have severe limitations in terms of reflecting the true economic performance and financial position of a company during a period of accelerated inflation. The full effect of inflation on the operations of a company is difficult to measure. We believe the problem to be important and far reaching.

Submission of supplementary inflation adjusted statements is now recommended in the United Kingdom and guidelines have been issued by recognized accounting associations in the United States and Canada. Accordingly, the following supplementary inflation adjusted financial statements attempt to show the effect that inflation has had on the financial results of the company.

We have used the price-level adjusted method since it is an accepted method for which reasonably consistent procedures have been established. Historical figures are translated into dollars of current purchasing power as at December 31, 1974 by use of a single price index. When referring to these statements it must be understood that the index applied is general and does not specifically deal with the rate of inflation which we have experienced in all sectors of our business. Generally, however, these statements tend to reflect more realistically than the historical statements, the earnings, asset values and shareholders' equity in terms of current dollars. The statements indicate the following:

(a) Real earnings are reduced due to inventory profits and higher depreciation resulting from valuation of fixed assets in current dollars. This reduction amounts to close to $11 million, comprised of higher depreciation of $7 million, and inventory profits of close to $4 million.

(b) Reduction in real earnings from these factors is not allowed as a tax deduction. Consequently, the effective tax rate is increased to 57 percent. If our earnings had been lower, that effective rate would have been even higher. It is a fact that inflation increases the effective rate of tax on corporations. This has great importance in terms of liquidity, dividends and earnings available for plant replacement, let alone expansion.

(c) The rate of return on assets employed is shown to be 11 percent on the inflation adjusted statements based on earnings after taxes (before extraordinary credit). If the extraordinary write downs made in 1971 and 1973 with respect to the sulphite mill and the reorganization were eliminated, the rate of return would be below six percent.

Method of Conversion

Fixed assets, inventories and capital stock items have been restated to current dollars by applying to such figures factors which reflect the changes in the purchasing power of the dollar between the respective dates of the original transactions and December 31, 1974. The conversion factors used are based on the Consumer Price Index.

Other assets and liabilities as at December 31, 1974 do not require restatement. The amounts are fixed by contract or otherwise and are therefore already expressed in terms of current purchasing power. Such assets and liabilities, known as monetary items, include cash, accounts receivable, current liabilities and long term debt.

The monetary items at the previous year-end are converted to the purchasing power of the dollar at December 31, 1974 by applying a factor based on the index at December 31, 1973 and the index at December 31, 1974.

Attempt to Adjust Results and Financial Position for Inflation

according to procedures noted on the opposite page.

Adjustments for Year

The following is a summary of adjustments required to restate 1974 net earnings from a historical basis to a current dollar basis:

	(Millions)
Net earnings on a historical basis	$ 50.9
Adjustments to convert to current dollar basis	
Additional depreciation based on cost of fixed assets valued in current dollars (not a replacement value)	(7.0)
Additional charge from restating inventories at the beginning and end of the year in current dollars	(3.9)
Gain due to the effect of inflation on net monetary liabilities, excluding long term debt	.5
Gain resulting from the effect of price-level changes during the year on sales and expenses	2.6
	43.1
Gain due to the effect of inflation on long term debt	7.6
Net earnings on a current dollar basis	$ 50.7

	(Millions) Current Dollar Basis	Historical Dollar Basis
Results for 1974		
Net sales	$ 201.8	191.5
Earnings before taxes and extraordinary item	47.0	54.6
Provision for income taxes	27.0	25.6
Earnings before extraordinary item	20.0	29.0
Per share	*$ 1.64*	*2.38*
Extraordinary item	23.1	21.9
	43.1	50.9
Gain due to the effect of inflation on long term debt	7.6	—
Net earnings	$ 50.7	50.9
Per share	*$ 4.16*	*4.17*

	(Millions) Current Dollar Basis		Historical Dollar Basis	
	1974	**1973**	**1974**	**1973**
Financial Position at December 31				
Current assets	$ 88.3	63.8	87.6	56.4
Investment and deposits	4.0	3.4	3.4	2.6
Fixed assets	415.5	406.0	263.6	252.3
Accumulated depreciation, amortization and depletion	(329.8)	(317.0)	(206.4)	(198.1)
	178.0	156.2	148.2	113.2
Current liabilites	35.0	48.6	35.0	43.2
Long term debt	54.3	69.0	54.3	61.4
Shareholders' equity	88.7	38.6	58.9	8.6
	$178.0	156.2	148.2	113.2

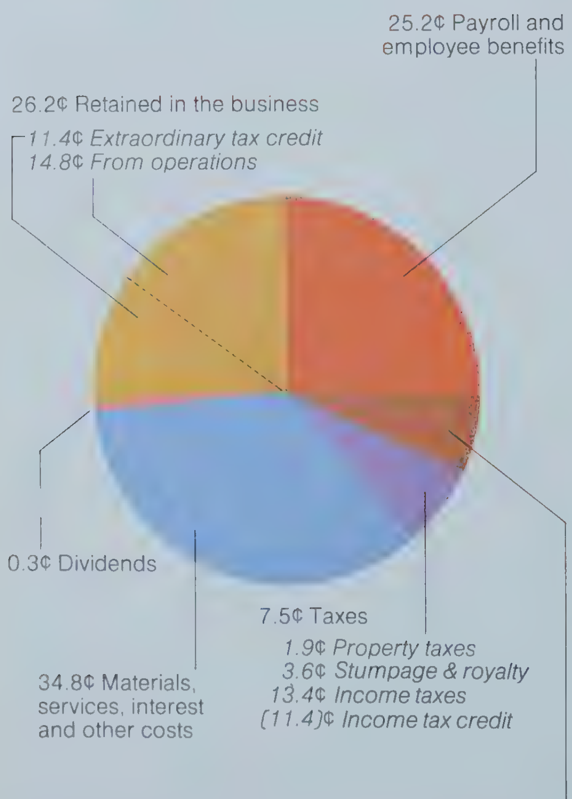
Canadian Cellulose Company, Limited and subsidiaries

Ten Year Review

	1974
Earnings (millions)	
Net sales	$191.5
Earnings (loss) before undernoted items	54.6
Provision for income taxes	25.6
Earnings after taxes	29.0
Minority interest	—
Earnings (loss) before extraordinary items	29.0
Extraordinary items	21.9
Net earnings (loss)	$ 50.9
Per share	
Earnings before extraordinary item	$ 2.38
Net earnings	4.17
Cash flow from operations before extraordinary item	3.29
Cash flow from operations	5.08
Dividends	.05
Financial position (millions)	
Working capital	$ 52.6
Fixed assets	263.6
Accumulated depreciation, amortization & depletion	(206.4)
Other assets	3.4
	113.2
Long term debt	54.2
Deferred income taxes	.1
Minority interest	—
Shareholders' equity	58.9
	$113.2
Changes in financial position (millions)	
Sources: Cash flow from operations	$ 61.9
Other, including long term financing	.1
	62.0
Applications: Fixed assets	14.6
Dividends	.6
Long term debt	7.1
Other	.3
	22.6
Increase (decrease) in working capital	$ 39.4
Production and Other statistics	
Kraft pulp (thousands of short tons)	409
Sulphite pulp (thousands of short tons)	156
Lumber (millions of board feet)	243
Logs (thousands of cunits)	1,297
Employees at year end	3,197

Note: *Comparative data for 1972 and prior is that of Columbia Cellulose reorganization at June 29, 1973 renders this comparison with Columbia*

Disposition of 1974 sales dollar



1973	1972	1971	1970	1969	1968	1967	1966	1965
133.8	118.8	83.5	83.5	103.3	88.2	67.5	64.4	65.5
13.3	(7.9)	(19.0)	(7.7)	1.4	(9.8)	(16.6)	(.6)	6.7
6.2	.1	(2.5)	(3.8)	.8	(.3)	(3.2)	1.5	3.2
7.1	(8.0)	(16.5)	(3.9)	.6	(9.5)	(13.4)	(2.1)	3.5
—	—	(.5)	—	—	—	2.6	1.4	—
7.1	(8.0)	(17.0)	(3.9)	.6	(9.5)	(10.8)	(.7)	3.5
5.2	—	(31.8)	—	.8	—	—	—	—
12.3	(8.0)	(48.8)	(3.9)	1.4	(9.5)	(10.8)	(.7)	3.5
.58								
1.01								
1.54								
1.97								
—								
13.2	(32.6)	19.5	12.0	20.6	24.4	29.5	20.5	34.2
252.3	253.1	245.9	241.8	237.2	227.4	225.4	220.6	170.5
(198.1)	(125.3)	(116.9)	(81.7)	(75.6)	(67.4)	(57.6)	(52.4)	(46.8)
2.6	3.5	4.4	4.5	2.3	2.6	4.4	4.3	28.2
70.0	98.7	152.9	176.6	184.5	187.0	201.7	193.0	186.1
60.5	71.2	117.4	103.6	102.8	105.4	125.5	114.3	105.3
.9	—	—	2.7	6.5	6.4	6.6	9.8	8.7
—	29.9	29.9	15.5	15.5	15.5	15.0	2.6	4.0
8.6	(2.4)	5.6	54.8	59.7	59.7	54.6	66.3	68.1
70.0	98.7	152.9	176.6	184.5	187.0	201.7	193.0	186.1
24.0	2.8	(8.0)	3.0	11.9	1.9	(6.8)	6.2	12.3
42.3	1.6	35.3	13.1	2.7	17.4	32.7	40.5	37.4
66.3	4.4	27.3	16.1	14.6	19.3	25.9	46.7	49.7
9.5	10.2	12.1	11.2	12.7	4.0	11.1	51.9	32.1
—	—	.5	1.0	1.5	.5	1.0	1.0	2.3
7.3	46.2	7.2	9.9	4.2	4.3	4.8	4.1	—
3.7	.1	—	2.6	—	15.6	—	3.4	.5
20.5	56.5	19.8	24.7	18.4	24.4	16.9	60.4	34.9
45.8	(52.1)	7.5	(8.6)	(3.8)	(5.1)	9.0	(13.7)	14.8
378	421	392	338	408	384	270	187	178
140	154	143	130	168	174	158	155	181
254	249	232	150	133	127	86	118	114
1,451	1,095	1,165	1,001	1,368	1,214	1,087	848	776
3,022	2,951	2,748	2,649	2,738	2,840	2,913	2,963	2,665

ompany, Limited and subsidiaries. Per share information is not shown other than for 1974 and 1973 since the
llulose inappropriate.


Canadian Cellulose Company, Limited
WOODS OPERATIONS
PULP OPERATIONS
LUMBER OPERATIONS
ALASKA
Nass River
Skeena River
ALBERTA
TO JAPAN
KITWANGA
PRINCE RUPERT
TERRACE
KITIMAT
BRITISH COLUMBIA
TO U.S.A. & EASTERN CANADA
Columbia River
Fraser River
TO EUROPE
TO JAPAN
REVELSTOKE
NAKUSP
TO U.S.A. & CANADA
VANCOUVER
Corporate Office
TO VANCOUVER & EXPORT
CASTLEGAR
TO U.S.A. & MEXICO
U.S.A.
TO EUROPE & SOUTH AMERICA

The letter to Shareholders and Employees, the Operations Review and the Highlights contained in this Annual Report together constitute the Directors' Report to the members for the year 1974.

Canadian Cellulose Company, Limited